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SIPDIS

DEPT PASS TO USTR BENNETT HARMAN AND RUSSELL SMITH

E.O. 12958: N/A
TAGS: ETRD EINV ECON EAGR EC
SUBJECT: ECUADOR UPDATE FOR ATPA REPORT

REF: STATE 18743

¶1. Per reftel request, we provide the following information for the update to the ATPA report for Ecuador. A Microsoft word version of the information below has been sent separately via email to USTR.

¶2. Ecuador Population: 13,027,000 (2004 est.)
National Product per capita: $1,447 (2004 est., using year 2000 USD)
Source: Central Bank of Ecuador

¶3. 2004 Trade Statistics (thousands $)
U.S. Imports from Ecuador: $4,284,667
U.S. Exports to Ecuador: $1,665,883
U.S. Trade Balance: -$2,618,784
Source: U.S. Department of Commerce (Tradestat)

¶4. Effect of the ATPA/ATPDEA: Despite the ATPA's provision of duty-free entry to a wide range of Ecuadorian products, the country's exports remain concentrated in petroleum and a handful of other traditional products. Estimated figures for 2004 indicate that petroleum and its derivatives accounted for 67% exports to the United States. One of the most economically significant nontraditional export products that has benefited from duty-free treatment under ATPA is cut flowers. In 2004, Ecuador exported $201.1 million in cut flowers to the United States. Exports of nontraditional products show a steady upward trend with exports to the United States increasing considerably from $719.3 million in 2002 to $876 million in 2004. Some products, including broccoli and pineapple, experienced double digit export increases to the U.S. in 2004. Exports of some traditional products have increased since 2000. Coffee exports to the U.S. rose by 47% in 2004 reaching $8.7 million dollars. Shrimp exports reached a peak of nearly $174 million dollars in 2004. Cacao exports to the United States also increased substantially in 2003, leveling off at $39 million in 2004. On the other hand, banana exports have declined since 2002. In 2004 banana exports reached 228.1 million to the U.S. -- down from $256.4 million in 2002. Ecuador expects to significantly increase its exports of tuna in pouches due to the inclusion of the product in the ATPDEA. Source: Central Bank of Ecuador

¶5. Foreign direct investment (FDI) has risen moderately over the last few years. Stock of U.S. FDI in Ecuador in 2003 was 1.4 billion, up from 1.28 billion in 2002. Most of the increase is associated with the oil sector. FDI in other sectors remains modest and is focused on financial services, food processing, telecommunications, the chemical and pharmaceutical industries, and machinery and vehicle manufacturing. For Ecuador to take full advantage of the possible investment benefits associated with the ATPA, it will need to improve its investment climate through providing greater transparency and certainty for foreign investors.

¶6. Expropriations: While cases of expropriation have been infrequent, two foreign investors have outstanding claims based on land and squatter disputes. Under Ecuadorian law, individuals have the right to petition a judge to establish the appropriate price for expropriated holdings. The Agrarian Development Law restricts the grounds for expropriation of agricultural land and provides for adjudication of disputes in the courts. Though foreign and domestic investors are treated equally under the law, the extent to which investors and lenders receive prompt, adequate and effective compensation varies from case to case. Under Ecuador's Bilateral Investment Treaty with the United States, expropriation can only be carried out for a public purpose, in a nondiscriminatory manner, and upon payment of prompt, adequate and effective compensation.

¶7. Arbitral Awards: The U.S.-Ecuador Bilateral Investment Treaty (BIT) provides for international arbitration of disputes at the investor's option. Ecuador is a member of the International Center for the Settlement of Investment Disputes (ICSID). A U.S. company received an arbitral award in a dispute over the company,s eligibility for value-added tax refunds in 2004. Shortly after the award was announced, Ecuador,s Solicitor General (Procurador) launched an investigation of the company. He subsequently declared there were legal grounds to void the company,s contract and seize its considerable assets in Ecuador. The Procurador does not

have the final word in the matter and the case is currently being reviewed by other GOE entities. The Procurador has also sought a judicial review of the award decision, which is still pending. There are other high profile legal cases brought by and against foreign companies. In early 2005, Ecuador modified the Arbitration and Mediation Law to prohibit international arbitration if the national interest could be affected. This modification appears to conflict with the terms of the BIT with the U.S., and at a minimum will create confusion among investors regarding their right to arbitration. It also contributes to investors, negative impressions about the lack of legal due process in the country.

¶8. Reverse Preferences: The U.S. Government has no indication that Ecuador has granted such preferences to the products of a developed nation. Furthermore, Ecuador is a member of the World Trade Organization (WTO) and, accordingly, is bound by the most-favored-nation provisions in the WTO Agreements.

¶9. Intellectual Property:

a. Ecuador's intellectual property regime is governed by the "Law on Intellectual Property" adopted in 1998. The law provides criminal and administrative relief to right holders. Ecuador has ratified the Berne Convention for the protection of literary and artistic works, the Geneva Phonogram Convention, and the Patent Cooperation Treaty. Ecuador is also bound by the Andean Community Decision 345 (Common Regimen for the Protection of Rights of Vegetable Varieties Holders), Decision 351 (Common Regimen Regarding Author Royalties and Related Rights) and Decision 486 (Common Regimen Regarding Industrial Property). Decision 486 improves intellectual property protection by expanding the definition of patentability and strengthening data exclusivity. In April 2001, the U.S. Trade Representative (USTR) removed Ecuador from its Special 301 Watch list to reflect improvements in Ecuador's intellectual property regime. However, weakened enforcement (particularly in the area of pharmaceuticals) led to Ecuador's re-listing in 2003. Ecuador made a public commitment to apply the WTO TRIPS agreement from the date of its accession to the WTO.

b. In 2004, the Andean Community confirmed the legality of a Colombian decree reinforcing data exclusivity rules and intellectual property rights. This decision removed key conflicts between Andean Community rules and Ecuador,s WTO commitments, theoretically reinforcing the legal protections for intellectual property rights. However, Ecuador continues to issue sanitary registrations to illegal copies of patented products, violate data confidentiality, and ignore violations of its WTO commitments and its own intellectual property law.

c. Enforcement against intellectual property infringement remains a serious problem in Ecuador. The national police and the Customs Corporation of Ecuador (CAE, by its Spanish initials) are responsible for carrying out IPR enforcement orders, but it has sometimes been difficult to have court orders enforced. There is a widespread local trade in pirated audio and video recordings, computer software and counterfeit activity regarding brand name apparel. On the other hand, local registration of unauthorized copies of well-known trademarks has been reduced. Some local pharmaceutical companies, who produce or import pirated drugs, have successfully blocked improvements in patent protection and enforcement of data protection.

d. The IPR law extends patent protection for 20 years from the date of filing. Patenting of pharmaceutical products is permitted. Compulsory licensing is relatively limited. In infringement cases, the burden of proof lies with the alleged infringer. The law also provides patent protection for new drugs. Although Andean Community Decision 486, issued in late 2000, represents a significant improvement over Decision 344, it still does not provide adequate protection for "second use" patents.

e. Producers of branded pharmaceuticals are concerned that the "Law on Generic Drugs", which was passed in 2000, enshrines discrimination against branded pharmaceuticals into law. The law mandates that Government entities buy only generic drugs. The law also lowers drugstore gross profit margins on branded medicines to 20%, while maintaining the margins for generic drugs at 25%. Under the law, drugstores are also required to devote a certain percentage of shelf space to generic pharmaceuticals. The GOE is proposing to further reduce allowable profit margins on pharmaceutical sales.

f. Printed and recorded works are in theory protected under the IPR law for the life of the author plus 70 years. Computer programs and software are also protected. However, pirated CDs, DVDs and computer software (at prices beginning at $1) are widely sold, with apparent impunity. Ecuador's Education Law appears to allow educational institutions to

copy software without regard to such protections. The Government has taken no action to correct this problem.

g. Trademark registration is permitted for renewable 10-year periods, but registration may be canceled if the mark is not used in the Andean region for a period of three years. The IPR law provides protections for well-known trademarks. A trademark registration cannot be voluntarily surrendered without the consent of the licensee.

h. The IPR law provides protection for industrial designs and extends protection to industrial secrets and geographical indicators. Semiconductor chip layouts are protected. Plant varieties and other biotechnology products are also, in theory, protected. In 2004, U.S. Customs seized and destroyed cut-flower exports to the United States by Ecuadorian companies that were not paying royalties to holders of plant variety rights.

i. The Ecuadorian Intellectual Property Institute (known by its Spanish acronym IEPI) was established in January 1999 to handle patent, trademark and copyright registrations on the Ecuadorian Government's behalf. IPR enforcement has improved, although piracy remains. The Ecuadorian National Police and the CAE are responsible for carrying out IPR enforcement orders, but they often do not recognize the authority of, or enforce IEPI orders. Some foreign companies have complained that authorities have been increasingly reluctant to issue and carry out IPR enforcement orders. IEPI has reduced its enforcement efforts due to funding and staffing constraints and an apparent reduction in the Ecuadorian government's emphasis on IPR protection. Industry sources have also expressed concern about the premature dismissal of the former president of IEPI and the possible politicization of the institution.

¶10. Extradition: An extradition treaty was signed in Quito on June 28, 1872, and entered into force on November 12,
¶1873. A supplementary extradition treaty was signed in Quito on September 22, 1939, and entered into force on May 29,
¶1941. The treaties permit the extradition of U.S. citizens. A more modern extradition treaty would benefit both countries.

¶11. Workers, Rights:

a. The Labor Code provides for a 40-hour work week, 15 calendar days of annual paid vacation, restrictions on child labor, general protection of worker health and safety, minimum wages and bonuses, maternity leave, and employer-provided benefits. By law, companies must distribute at least 15% of pre-tax profits to their employees. Many employers rely on short-term outsourcing contracts since job tenure rules make it difficult to lay off permanent workers. New regulations restricting use of such contracts were issued in 2004.

b. Legal changes to modernize the country's Labor Code were passed by Congress in 2000 as part of omnibus economic reform legislation. However, the Constitutional Tribunal declared virtually all of the changes unconstitutional. Since then, efforts to reform Ecuador's antiquated labor laws have stalled.

c. Most workers in the private and parastatal sectors have the constitutional right to form trade unions and local law allows for unionization of any company with more than 30 employees. Private employers are required to engage in collective bargaining with recognized unions. The Labor Code provides for resolution of conflicts through a tripartite arbitration and conciliation board process. The Code also prohibits discrimination against unions and requires that employers provide space for union activities.

d. Some companies have taken advantage of the law that prohibits unions from organizing at companies that have less than 30 employees by sub-contracting with several shell companies, each of which has less than 30 workers. Under the Labor Code, these subcontracted workers have no legal right to freedom of association or right to bargain collectively with the companies that ultimately benefit from their labor, nor do they have legal protection against anti-union discrimination. New regulations restricting use of such contracts were issued in 2004.

e. Except for public servants and workers in some parastatals, workers by law have the right to strike. Legally striking employees are entitled to full pay and benefits and may occupy the premises under police protection, although there are restrictions on solidarity strikes. Most public sector employees are technically prevented from joining unions, but most are members of a labor organization and most labor actions are in fact illegal strikes by public employees. Although trade union political influence has declined in recent years, labor groups occasionally attempt to stage national strikes to protest economic reform measures.

f. In practice, employers that violate worker rights are seldom punished. Labor rights activists allege that violent tactics, which resulted in serious injury to workers, were employed to break a strike on a large banana plantation in ¶2002. In each of the last three years, at least 30 Members of the US Congress have signed a letter expressing Congressional concern about labor rights protections in Ecuador.

g. The Constitution and the labor code prohibit forced labor. The law also prohibits the employment of persons under the age of fifteen years old, except in special circumstances such as an apprenticeship. Enforcement of this provision is uneven, especially in rural communities. In the cities, many children under fifteen years old work in family businesses in the informal sector. The International Labor Organization estimated that 69,000 children ages 10 to 14, and an additional 325,000 young people ages 15 to 19, were working on plantations in 1999. These figures have dropped since 1999, but remain high according to the International Labor Organization,s report for 2004. Child labor is still common on plantations, large and small. In 2004, Ecuador hired child labor inspectors in an effort to combat the child labor problem.

h. Only a significant increase in wages, at best a distant prospect in a country where the average worker earns $5.74 a day, will keep families from sending their children out into the fields, labor advocates in Ecuador and in the United States say. But while rights activists regard such labor as unacceptable, many parents see it as a necessity.

i. The minimum wage appears inadequate to provide a decent standard of living for a worker and his or her family. Most organized workers in state industries and in the formal sector (private enterprises) earn more than the minimum wage and are provided other significant benefits through collective bargaining. The majority of workers work in the large informal sector, without recourse to the minimum wage or legally mandated benefits.

¶12. Economic Conditions: Ecuador adopted the U.S. dollar as its national currency in 2000 in response to the most serious economic crisis in its history. Dollarization, combined with recent responsible fiscal policies, has helped to tame inflation and bring the country back to positive growth. However, to sustain dollarization in the medium term Ecuador must enact structural economic reforms and improve its ability to compete in the global marketplace. Ecuador,s GDP grew an estimated 2.7 percent in 2003, and 6.6 percent, largely a result of increased oil exports and record high oil prices. (Source: Central Bank of Ecuador)

¶13. Market Access: Ecuador's accession to the WTO in 1996 was an important step in improving access to Ecuador's market. However, a number of trade barriers remain. For example, despite recent improvements, bureaucratic procedures required to obtain clearance for imports from the Government,s standards-setting body still appear to discriminate against foreign products. Also, corruption and inefficiency in the sanitary registration process have delayed and even blocked the entry of some agricultural imports from the United States.

a. Ecuador requires prior authorization from various government agencies, e.g., the Ministry of Agriculture (MAG) for importation of most commodities, seeds, animals, and plants. Also, the Ministry of Health must give its prior authorization (i.e., sanitary registration) before the importation of processed, canned, and packed foods as well as food ingredients and beverages, cosmetics and pharmaceutical products. Another administrative hurdle agricultural importers must overcome is the MAG,s use of &Consultative Committees8 (Committees). The Committees, mainly composed of local producers, often advise the MAG against granting import permits to foreign suppliers. The MAG often requires that all local production be purchased at high prices before authorizing imports.

b. Ecuador also continues to maintain a preshipment inspection (PSI) regime. Preshipment inspection by an authorized inspection company (both before shipment and after specific export documentation has been completed at the intended destination) results in delays far exceeding the time saved in customs clearance. Customs authorities sometimes perform spot-checks, causing further delays. These practices generally add six to eight weeks to shipping times.

c. When it joined WTO in January 1996, Ecuador bound most of its tariff rates at 30 percent or less. Ecuador,s average applied tariff rate is about 13 percent ad valorem. Since February 1995, Ecuador has applied a common external tariff (CET) with two of its Andean Community partners, Colombia and Venezuela. Although Ecuador has harmonized its tariff

schedule with the CET, it took numerous exceptions in order to maintain lower tariff rates on capital goods and industrial inputs. Agricultural inputs and equipment are imported duty-free.

d. Ecuador,s foreign investment policy is governed largely by the national implementing legislation for Andean Community Decisions 291 and 292 of 1991 and 1993. Foreign investors are accorded the same rights of entry as Ecuadorian private investors, may own up to 100 percent of enterprises in most sectors without prior government approval, and face the same tax regime. There are no controls or limits on transfers of profits or capital. There are no performance requirements, with the exception of the auto regime. A Bilateral Investment Treaty with the United States that guarantees access to binding international arbitration entered into force in May 1997.

e. Certain sectors of the economy are reserved to the state, although the scope for private sector participation, both foreign and domestic, is increasing. All foreign investment in petroleum exploration and development in Ecuador must be carried out under a contract with the state oil company. Ecuadorian law permits the sales of 51 percent of the state,s electrical sector facilities and telephone companies. Foreign investment in domestic fishing operations, with exceptions, is limited to 49 percent of equity. Foreign companies cannot own more than 25 percent equity in broadcast stations and are not permitted to obtain broadcast concessions. Foreign investors must obtain approval from the President and the National Security Council to obtain mining rights in zones adjacent to international boundaries.

¶14. WTO Agreements: Ecuador acceded to the WTO in January
¶1996. Ecuador has failed to meet deadlines for fulfilling some of its WTO obligations related to the elimination of non-tariff barriers. These include requirements for prior authorization for certain goods before the central bank can issue an import license, and Ministry of Agriculture denial of import permits for certain agricultural products in order to protect local producers. Ecuador is not complying with its commitments under the WTO,s Technical Barriers to Trade Agreement (TBT).

¶15. FTAA Participation: Ecuador chaired the FTAA negotiations process until the Quito Ministerial, held in November 2002, and continues to participate in the process. Ecuador,s FTAA negotiating positions are usually developed jointly with its Andean Community partners Ecuador, Peru, and Colombia are currently negotiating an FTA with the United States.

¶16. Subsidies or Other Requirements that Distort International Trade: Ecuador does not use export subsidies. It does maintain a drawback system to reimburse the cost of duties and taxes paid on raw materials and other inputs incorporated in products that are subsequently exported.

¶17. Trade Policies that Revitalize the Region: Ecuador acceded to the Andean Community in early 1993. Ecuador,s trade is gradually reorienting toward the Community. In 2003, the Andean Community absorbed 17.47 percent of Ecuador,s exports and provided 22.8 percent of its imports (Source: Central Bank of Ecuador).

¶18. Narcotics Cooperation: Ecuador has received full certification for its cooperation through 2002 with the United States on counter-narcotics issues under the Foreign Assistance Act, as described in the International Narcotics Control Strategy Report of March 2003. With the support of the U.S. Government, Ecuador maintains an active drug detection and interdiction program. Its programs focus on demand reduction, interdiction, training in police investigations and drug detection, information sharing and control of money laundering. A program initiated in 1996 targets modernizing the judicial system. However, Ecuador,s current money laundering law is largely ineffective and needs to be reformed. A proposal to reform the money laundering law was presented to the Ecuadorian Congress in 2004, but little progress has been made in getting it enacted.

a. The Government of Ecuador continues to work with the U.S. Government to reduce trafficking through Ecuador. Ecuador has criminalized the production, transport and sale of controlled narcotic substances. Although smuggling of precursor chemicals through Ecuador remains a problem, the Government of Ecuador is making efforts to monitor and control these chemicals. Nonetheless, it appears that, despite Ecuadorian efforts, transshipment of narcotics through Ecuadorian maritime and land routes to the United States is widespread.

b. The ATPA has played an important role in providing trade opportunities in agricultural industries in Ecuador. Such opportunities have provided the citizenry with jobs, thus deterring them from becoming involved in growing narcotics

crops and, consequently, preventing the entrenchment of narcotics trafficking in Ecuador. ATPA's contribution to the rapid growth of Ecuador,s cut flower industry has been particularly important. Cultivation of fresh fruits, vegetables and cereals in the highlands is also growing and offering similarly promising export and employment opportunities. Ecuador,s beneficiary status under the ATPA helps to create the conditions for such opportunities.

c. The successful development of more profitable agricultural industries in Ecuador will help prevent Ecuador from becoming a major coca-producing country. Ecuador's proximity to Colombia and Peru, the world's leading coca leaf and cocaine hydrochloride suppliers, warrants continued vigilance in preventing illicit crop cultivation in Ecuador.

¶19. Anti-Corruption: In international rankings, Ecuador has been reported to suffer from high levels of corruption. Judicial insecurity, impunity and lack of transparency in regulatory bodies and GOE-related entities are frequently cited as the root causes of corruption in Ecuador. Efforts at reform have had mixed results to date. There is an independent anti-corruption agency, but it is under funded and without legal teeth. There are few non-governmental institutions that fight corruption.

¶20. Government Procurement:

a. Ecuador is not a signatory to the WTO Agreement on Government Procurement. The Public Contracting Law, issued in 2001, regulates government procurement of goods, equipment, and services. Purchases made by the State-owned telephone and electric power distributors, and by military-owned companies are not required to follow this law. Foreign bidders must be legally represented in Ecuador. Ecuadorian companies and those of the foreign country sponsoring the bid may participate in public bids financed by government-to-government credits. Association with an Ecuadorian company is only required for the execution of government-to-government public works contracts and those that are carried out with direct or supplier credits. It is only for these types of contracts that the foreign company needs to retain at least double the capital of its Ecuadorian associate. Foreign contractors may not use national credit for the execution of their contracts.

b. Procurement by public invitation involves various steps. The government agency usually inserts announcements in newspapers and trade journals inviting potential suppliers to present bids for specific types of equipment or services desired. The interested party must purchase bid documents containing detailed information. The bids must be completed in Spanish, using the format specified by the inviting agency, and be delivered to the contracting agency in person.

c. Bidding for government contracts can be cumbersome, and competitors from other countries do not operate under the restrictions of the U.S. Foreign Corrupt Practices Act. There is no formal discrimination against U.S. suppliers.

d. Under the Public Contracting Law, the government requires either a bank-issued guarantee or an insurance guarantee to cover 5 percent of the contract, to ensure execution of the contract. (Military contracts, however, permit only bank-issued guarantees.) A guarantee of money advances made by the Government is also required from the supplier. Before a Government contract is approved, it must have authorization from both the Comptroller and Attorney General.

e. The Public Contracting Law prohibits government institutions from purchasing used equipment.

¶21. Counter-Terrorism: As did most Latin American nations in the wake of the September 11 attacks in the United States, Ecuador voiced strong support for U.S., Organization of American States and United Nations antiterrorism declarations and initiatives put forth in various international fora. During President Gutierrez,s February 2003 visit to Washington, he publicly proclaimed his desire to make Ecuador a strong ally in the fight against terrorism. Ecuador is making efforts to improve control of its borders. Other issues of concern include Ecuador,s weak financial controls, widespread document fraud and reputation as a strategic corridor for arms, ammunition and explosives destined for Colombian terrorist groups.
KENNEY